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Chimerica

by nickland @ Wednesday, 01 June 2011 17:10

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A new world order hits the buffers

"For nearly 30 years we have had two Global Strategies working in a symbiotic fashion that has created a virtuous economic growth spiral. Unfortunately, the economic underpinnings were flawed and as a consequence, the virtuous cycle has ended. It is now in the process of reversing and becoming a vicious downward economic spiral," writes Gordon T. Long, in a guest post at Zero Hedge. "One of the strategies is the Asian Mercantile Strategy. The other is the US Dollar Reserve Currency Strategy."

The system that Long sees unraveling has been dubbed 'Chimerica' by Niall Ferguson and Moritz Schularick, in reference to the mythical hybrid beast of antiquity. Chimerica emerged through the dynamic coupling of the US and Chinese economies, dominating the wave of globalization in the post-command economy world. It has served as a powerful engine of development, spreading prosperity beyond the narrow enclave of the (Euro-American) 'First World' and facilitating the global roll-out of digital network technologies, from personal computing and mobile telephony to the Internet. In recent years, however, its unsustainable features have become prominently visible.

Stripped to its fundamentals, Chimerica amounted to something akin to an informal geopolitical 'deal' that simultaneously promoted the international status of the US Dollar and domestic Chinese industrialization. The principal financial mechanism was the recycling of Chinese trade surpluses into US Treasury Bonds, in a process that accentuated Chinese competitiveness (by restraining the rise of the Yuan) and suppressed US inflation (preserving the credibility of the USD). This enabled Chinese industrial expansion to proceed at a far greater speed than its domestic market could have supported, whilst providing US governments with the latitude to run a chronically loose monetary policy immunized against the prospect of currency collapse. The Chinese manufacturing and US banking sectors were the most obvious beneficiaries. Both prospered conspicuously.

As Niall Ferguson wrote in November 2008, in the early days of the world financial crisis:

"At the heart of this crisis is the huge imbalance between the United States, with its current account deficit in excess of 1 percent of world gross domestic product, and the surplus countries that finance it: the oil exporters, Japan and emerging Asia. Of these, the relationship between China and America has become the crucial one. More than anything else, it has been China's strategy of dollar reserve accumulation that has financed America's

debt habit. Chinese savings were a key reason U.S. long-term interest rates stayed low and the borr
that the age of leverage is over, 'Chimerica' -- the partnership between the big saver and the big sp

Having reached a state of crisis, Chimerica seems certain to unwind. This might occur either throug
that increases Chinese domestic consumption whilst reducing US deficit spending, or as a messy di
sudden demand contraction, currency wars, and escalating mutual recrimination. Whatever the eve
world order is an inevitable – which is to say, definitional – result.

Whilst Ferguson hedges his bets, Gordon Long spells out a specific and ominous forecast, in which
Chimerican globalization reverses into a vicious 'death spiral'. As 'debt saturation' closes down the
actions of the US Federal Reserve become manifestly ineffective, self-contradictory, and ultimately
process of currency destruction then begins in earnest. Long offers a useful checklist of milestones
(proceeding from financial, through economic, to political calamity):

1. A deteriorating US dollar

2. Rising US interest rates

3. Sustained and chronic US unemployment

4. Asian inflation, especially in food where 60% of Asian disposable income is spent

5. Pressures on Asian currency pegs

6. Collapsing values of US Reserve holdings

By the end of this process, the world will have been violently catapulted out of a financial architectu
dominant monetary philosophy that has prevailed over the course of centuries.

"The eventuality of a fiat currency crisis is ordained and has been since the early warnings in 2007
insists. "The roadmap has been clear to all that actually wanted to look."

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